



# AMERICAN BAR ASSOCIATION

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**TESTIMONY**

**OF**

**RICHARD A. SHAW**

**CHAIR OF THE**

**AMERICAN BAR ASSOCIATION SECTION OF TAXATION**

**BEFORE THE**

**IRS OVERSIGHT BOARD**

**AT ITS**

**PUBLIC STAKEHOLDER MEETING**

**JANUARY 26, 2004**

Good afternoon. My name is Richard A. Shaw. I am Chair of the American Bar Association Section of Taxation and I appear before you today on behalf of the American Bar Association. My testimony represents the views of the ABA with the exception of those comments concerning Circular 230 which are presented on behalf of the Section of Taxation. Those comments have not been considered by the ABA House of Delegates or Board of Governors and should not be considered as Association policy.

The ABA appreciates the opportunity to appear before the IRS Oversight Board (the “Board”) today to discuss the important strategic issues facing the Internal Revenue Service (the “Service”). On behalf of the ABA, I want to thank the Chair and the Members of the Board for their efforts to improve tax administration and the tax system overall.

#### ABA Section of Taxation

The ABA is comprised of more than 400,000 members and the Section of Taxation has approximately 20,000 members. The Section of Taxation’s members include attorneys who work in law firms, corporations and other business entities, government, non-profit organizations, academia, accounting firms and other multidisciplinary organizations. As the country's largest and broadest-based professional organization of tax lawyers, one of our primary goals is to make the tax system fairer, simpler and easier to administer.

The Section’s members provide advice on virtually every substantive and procedural area of the tax laws, and interact regularly with the Service and other government agencies and offices responsible for administering and enforcing such laws. Many of our members have served in staff and executive-level positions at the Service, the Treasury Department, the Tax Division of the Department of Justice, and the Congressional tax-writing committees.

#### Overview

We appreciate the opportunity to provide input to the Board regarding the IRS strategic plan for the next five years. The responsibilities of the Service are certainly mammoth, given that the organization is required to collect nearly two trillion dollars per year to fund the obligations of the federal government. We

commend the Service and this Board for the efforts that have been taken since 1998 to make the Service an efficient, modern and responsive agency. We have long endorsed efforts to make it simpler for taxpayers to comply with their responsibilities and at the same time increasing all taxpayers' confidence that the taxes imposed by our laws are collected fairly and efficiently. Balancing service and enforcement is a difficult task, and continued improvement in both areas must remain high priorities of the Service.

We believe that two external factors play a significant role in the ability of the Service to continue to improve its efforts to serve taxpayers and enforce the tax laws. These are the overwhelming complexity of the tax laws and the need for adequate resources for the Service to effectively perform its mission. Although Congress must play a primary role in addressing both of these areas, we do believe that the Service and this Board can and should act aggressively to help move things forward.

#### The Need for Simplification

First, I would like to focus on the critical need for simplification. The ABA and its Section of Taxation have long been strong advocates for simplification of the Internal Revenue Code. The ABA has designated tax simplification as one of its top legislative priorities. In resolutions proposed by the Section of Taxation and passed by the full ABA in 1976 and 1985, the ABA went on record urging tax law simplicity, a broad tax base and lower tax rates. We have reiterated this position in testimony before the congressional tax-writing committees on numerous occasions. For a number of years, the Section of Taxation has worked with our colleagues at the AICPA Tax Division and the Tax Executives Institute on this important issue, with whom we have jointly released identical simplification proposals. We will continue these efforts and – working with Treasury, the Service and Congress, we remain optimistic that real steps can be taken to simplify the tax laws.

Complexity is at the root of several significant obstacles to efficient and effective administration of the tax laws. First, as the National Taxpayer Advocate and others have well documented, the scope and complexity of the tax laws make it virtually certain that taxpayers will face procedural, technical and

bureaucratic obstacles in meeting their tax obligations. This not only creates problems on the front end, when taxpayers attempt to prepare and file returns, but also at the back end, when errors rooted in complexity result in audits and controversy with the Service. Second, as the staff of the Joint Committee on Taxation documented in their comprehensive study on tax simplification released in April 2001, complexity has materially reduced taxpayers' perceptions of fairness of the federal tax system by creating disparate treatment of similarly situated taxpayers. Although perceptions – and their impact – are difficult to measure, it is difficult to imagine how taxpayers or Congress can see the Service as an efficient, modern and responsive agency if they do not perceive the tax law itself to be fair. Third, as we have seen in recent years, tax law complexity creates opportunities for technical manipulation of the tax laws – often in ways never contemplated by Congress. Exploitation of ambiguities created by unnecessary complexity aggravates the perception problem. This forces the Service to divert resources from working with compliant taxpayers on legitimate issues to pursuing enforcement with aggressively noncompliant taxpayers.

Of course, we recognize that simplifying the tax law requires Congress to make difficult choices. This is particularly true when, as now, the political realities of the fiscal balance limit the ability to simplify in a manner that reduces revenue.

We appreciate that the Treasury Department and the Service have stepped up their efforts in recent years to work towards simplification through the regulatory process and we are committed to work with them to continue such efforts. We also commend the Service for the steps taken since 1998 to streamline the administrative system and improve the way the Service interfaces with taxpayers. We applaud efforts underway to redesign the examination and appeals processes to make them work more efficiently for both taxpayers and the Service. However, more can be done in the regulatory and administrative areas. A cornerstone of the IRS strategic plan for the next five years must be a meaningful effort to simplify the tax law itself and the Service's procedures for interacting with taxpayers.

The Service's efforts to refine its modernization program should consistently consider the necessity for quality and efficiency in dealing with taxpayers. The lack of efficiency is evidenced by the inability of the system to satisfy adequately the statutory and regulatory objectives of the Offers-in-Compromise program. Taxpayers should not be stranded in compliance limbo while offers take more than two years to be processed through Appeals.

Prompt issuance of guidance advances the goal of simplification by reducing ambiguity and uncertainty. This can take the form of formal Revenue Rulings and Revenue Procedures that provide clarity and simplify the administration of complex and ambiguous laws and regulations, as well as prompt public releases that provide guidance on new tax legislation. In addition, procedural simplification can be advanced by a strong program to modernize forms and instructions to make them more readily understandable and manageable to the average taxpayer.

Additional training is essential so that auditors and appeals officers are better able to explain and apply complex tax laws in a fair and just manner. Taxpayers and the system are not served well by Service Center communicators who are correct on complex tax laws only 70 percent of the time.

In addition to these regulatory and administrative steps, we believe there is a second strategy that can and should be given greater attention. This deals with the need for legislation. Although the Service and this Board are not charged with writing the tax laws or even with recommending particular ways to simplify them, the Service is well-equipped to understand the problems caused by complexity. The Service and the Board must actively educate Congress and the public on how complexity adversely impacts the Service's ability to achieve its mission.

#### The Need for Adequate Resources

We have constantly championed the need to provide the Service with adequate resources to perform its mission. The recent announcement of organizational changes facilitated by the efficiencies of

electronic filing, consolidation of certain back-office processing functions, and other technology gains are proof that the underpinnings of the Restructuring Act are bearing fruit. Unfortunately, we expect that there is only so much that can be achieved in this manner.

To do more, two legislative problems must be addressed. First, in light of the multiple demands placed on the Service – which seem to increase each time Congress approves another revenue bill – we fear that the Service will never have sufficient funding to properly address those demands until serious steps are taken to address complexity in the law. Stated differently, we believe that the ability of the Service to do more with less will be vastly improved if Congress takes dramatic action to simplify the tax code.

Second, we continue to believe that the nature of the annual appropriations process hinders the ability of the Service – or any other federal agency for that matter – to maintain a constant focus on its strategic plan. While we recognize that this is a matter to be addressed by Congress, it must be reminded of the detrimental impact of stop and start programming. We understand that Congress has considered multi-year budget planning on some of the modernization efforts, and we would urge the Service and this Board to work with the Appropriations Committees to expand those concepts to better address some of the agency's personnel needs.

Again, we recognize that the ability of the Service to influence the appropriations is somewhat limited. However, we believe that the Board has a duty to bring this issue to Congress and other interested parties. Thus, we would recommend that the Board take whatever steps it can to assist the Service in this regard.

In summary on these issues, our primary message is the need for the Service to devote its strategy, personnel and resources to promote simplification in the administration of the tax laws and to provide information and guidance to Congress that will lead to greater simplification. The integrity, fairness and equity of the tax system require a concerted effort to obtain simplification.

### Additional Items for Consideration

The Tax Section believes that continued improvement is necessary in both service and enforcement, as well as in the maintenance of the proper balance between the two.

First, the Service must continue its efforts to encourage tax practitioners to help promote compliance. The July 26, 2002 amendments to Circular 230 are a positive step, as are the changes to the Office of Professional Responsibility. We strongly recommend a substantial increase in the personnel and resources allocated to the Office of Professional Responsibility. The December 30, 2003 proposed tax shelter opinion revisions to Circular 230 are also a major step in the right direction. The Section of Taxation recommends that strong, fair and equitable procedures be established to assure compliance with Circular 230 regulations as they become final.

As tax lawyers, we recognize the professional ethical responsibility of lawyers to the system, both individually and collectively through the Section of Taxation, and we are working with the Treasury Department and Service in this regard. We are committed to doing our part to help restore public confidence in the tax system. To that end, we are addressing, on a priority basis, the standards of tax practice embodied in ABA guidance. We look forward to working with this Board, the Treasury Department and the Service to create an environment in which tax professionals can maintain the highest ethical standards in delivering timely, accurate and helpful advice to their clients.

Second, the Service must continue its efforts to develop reliable, up-to-date, cost effective means of measuring compliance. Current, reliable data on non-compliance is critical as an information base to enable the Service to properly balance its efforts to educate taxpayers to comply, and to better target enforcement efforts on those who do not. The National Research Program is an important step in this process, and we encourage the Service to continue such efforts to develop useful compliance data through methods designed to minimize burden on taxpayers.

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The ABA hopes that the foregoing observations and suggestions are helpful to this Board in discharging its responsibilities. We would be happy to meet with you to further discuss these views or any other matters.

Thank you.